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# Interim Report on a Study of the Impact of Potential Free Trade in Textiles and Clothing Between Canada and the United States

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Government  
of Canada

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Textile and  
Clothing Board

Commission du  
textile et du vêtement

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Regional Industrial  
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Expansion industrielle  
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## NEWS RELEASE

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For release

IMMEDIATE

Subject

INTERIM REPORT ON IMPACT OF FREE TRADE IN  
TEXTILES AND CLOTHING RELEASED

RIE 41/84

OTTAWA, February 14, 1984 -- Industry Minister Ed Lumley today announced that the Textile and Clothing Board has released the interim report he had requested of a Study of the Impact of Potential Free Trade Between Canada and the United States in Textiles and Clothing.

The report summarizes reactions of 80 industry, labour and consumer representatives who submitted briefs to the Board at hearings held during November and December 1983 in Montreal, Toronto, Halifax, Winnipeg, Vancouver and Ottawa.

Mr. Lumley said the reactions from the representatives on the free trade issue varied from total rejection to immediate acceptance depending on, for example, the degree of specialization of their operations, whether they were subsidiaries of U.S. firms, whether they were producing under licence from a U.S. firm, whether they were already exporting to the U.S., whether they were importing raw materials from the U.S. and whether their products were subject to a U.S. tariff higher than the corresponding Canadian tariff.

All participants agreed that if free trade were to be implemented in the textile and clothing sector, it would be necessary to have a transition period, to harmonize customs regulations of both countries and for government to provide assistance to obtain in-depth knowledge of the U.S. market and to restructure their production facilities.

Mr. Lumley said the Board will continue its examination of the issue and will submit a final report to him in April 1984. This report will also be reviewed by the recently established Textile and Clothing Industries Task Force which is formulating and recommending a long-term development strategy for the sector to the federal government.

Canada

The Textile and Clothing Board reports to the Minister of Regional Industrial Expansion and conducts enquiries, monitors and produces reports on the potential harm of clothing imports on Canadian producers, the adjustment plans of Canadian producers who have alleged injury from imports, progress made by producers in implementing adjustment and restructuring plans, the technical and production capabilities of Canadian producers, the effect of protection measures implemented on Board recommendation, specific economic and technical issues and market development. The Board also maintains a watching brief on actions taken under the Arrangement Regarding Trade in Textiles and the General Agreement on Tariffs and Trade (GATT).

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## INTRODUCTION

In his letter of June 6, 1983, the Minister of Industry, Trade and Commerce requested, pursuant to Section 20 of the Act creating the Textile and Clothing Board, that the latter undertake a study of the economic impact of the potential mutual elimination of tariff and non-tariff barriers to trade between Canada and the United States for textile and clothing products.

In accordance with the Minister's directives the study should be aimed at determining the potential impact of the removal of barriers on productivity, competitiveness, investment, employment and national and regional industrial structures. It should take into account existing institutional and corporate factors, but should not touch on the negotiability aspects of a free trade zone, nor should it consider the international implications of such an arrangement.

On August 6, 1983, that is immediately after the reopening of plants following their annual holiday shutdown period, the Board published a notice in the Canada Gazette that it was undertaking this study, and distributed this notice to a large number of associations and firms in the textile and clothing sectors. The notice stipulated that written briefs on the subject be submitted not later than October 31, 1983, and that hearings relating to the study would be held in November of the same year.

The Board received 45 written briefs, and 74 participants<sup>1</sup> appeared before the Board during private hearings which were held between November 7 and December 8, 1983 in Ottawa, Halifax, Montréal, Toronto, Winnipeg and Vancouver.

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<sup>1</sup> See list in appendix I.

The Board also undertook additional research carried out either by its own personnel or by outside consultants.

This report, which has been prepared immediately after the hearings were completed, is only a brief preliminary report summarizing the positions taken by the participants in their written briefs and in the opinions expressed during the hearings. This preliminary report has been prepared pursuant to the wish expressed by the Minister to receive a report before the end of 1983.

A final report combining the results of research carried out by the Board and the information contained in the briefs and obtained during the hearings will be presented to the Minister in April 1984.

A. The free trade area and its advantages

The free trade area under consideration in this study would include two countries, Canada and the United States, and would cover two large product groups, textiles and clothing. The two countries would eliminate the barriers to trade for these two product groups, and these would be traded freely, without tariffs nor significant non-tariff barriers.

The free trade area would normally cover only the products made in one or the other of the partner countries. Products from third countries not party to the sectoral free trade arrangement would continue to be subject to tariffs and, where applicable, to restraint measures as applied at present by the two countries. Any free trade arrangement would therefore require a definition of what can or cannot be considered a product of one or the other country, and should specify the minimum domestic content for each product. This domestic content is generally expressed as a given percentage of the production costs incurred in either

participating country.<sup>2</sup>

The advantages of such an arrangement were easily identified by the participants. Canadian producers clearly perceive the advantage represented by a population ten times larger than that in their present market, and with a per capita disposable income slightly greater than that of the Canadian population.

The elimination of tariff barriers would allow greater access to numerous intermediate products, thereby contributing to lower production costs while assuring a much wider choice of intermediate products than is available at present to the Canadian producers.

There are numerous possibilities for Canadian firms to specialize in the event that a free trade area is established between Canada and the United States.

In this respect two major routes for specialization have been identified by the participants: specialization in certain basic product lines, and specialization in certain niches of high quality products.

Progressive specialization in basic products leads to economies of scale, that is, much longer production runs than at present. Economies of scale increase labour productivity as well as productivity of the equipment, thus contributing significantly to lower production costs.

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<sup>2</sup> In the automotive trade pact between Canada and the United States this percentage is set at 50 per cent.



Specialization in fewer products also makes possible a reduction of raw material and finished product inventories, and contributes to a more efficient use of the working capital.

Specialization in niches of high quality products means that producers, generally operating in the higher price brackets, could specialize in products requiring highly skilled labour, without having to produce also at lower quality levels as they must do at present because of the small size of the market for high quality products. A free trade area would provide a sufficiently large market for these products, thus eliminating the problems of mixing production at two levels of quality. In addition to allowing for greater productivity, this specialization in niches of high quality products would also allow significant reductions in raw material and finished product inventories.

Garment producers recognize that free trade could mean a larger number of retailers to sell to, and greater availability of fabrics. One of the traditional complaints of garment producers has concerned the high degree of rationalization of the primary textile industry and the resultant limitation in fabric availability, and the great concentration of retail trade. Free trade in textiles and clothing would mean that these producers would have access at the same time to a larger choice of fabrics, a larger number of sources of supply, and more outlets to market their products.

With regard to consumers, free trade would mean for them a greater selection of products at lower prices.

The free trade area suggested for the textile and clothing sectors involves greater coverage than the one involving the automotive sector. In the case of automotive products, only the producers of these products are allowed to import them duty free, while in the case of

textiles and clothing, everybody would be allowed to import duty free including retailers and consumers. The free trade area would therefore increase competition between domestic products and duty free imported products at every stage from the fiber producer to the consumer.

Therefore, in principle, free trade would have several advantages for both producers and consumers.

B. Some problems related to potential free trade in textiles and clothing

It can be said that textile and clothing industry structures in both Canada and the United States are largely similar. In fact, the product ranges are about the same, the technologies used are similar, and the size distribution of firms in both countries indicates a predominance of small and medium size firms and family-owned operations, except, of course the man-made fibre producers and the manufacturers of standardized clothing items (such as men's shirts and pants) among which are some multinational firms.

The apparent similarity of these industry structures could, in theory, justify the conclusion that a free trade area in these sectors would facilitate greater specialization and consolidation into larger and possibly more viable production units.

Nevertheless, numerous participants view potential free trade with some apprehension. In their written and oral presentations they have expressed the reasons for their apprehension.



1. While wages paid in Montreal and Toronto are close to those paid in New York, there are large areas in the United States where wages paid are significantly lower than in Canada. This is the case in Georgia and the two Carolinas for the textile industry, and the southeast and southwestern regions of the United States for the clothing industry. It should also be mentioned that in these same regions the degree of unionization is much less than in Canada, and labour regulation is significantly less restrictive.

Further, during the last few years, the spread between direct and indirect wages paid in Canada and those paid in the United States in these industries has widened considerably, and the differences in wages would be even more pronounced except for the depreciation of the Canadian dollar. Finally, it must be pointed out that any subsequent rise of the Canadian dollar in relation to the United States dollar would reduce further the competitive ability of Canadian producers against their potential competitors in the United States.

2. In addition to this wage disadvantage, the costs of building plants in southern United States are lower than in Canada. This difference, which has been calculated at about 35 per cent, results in part from lower wages in the construction trade, and in part also because of less stringent requirements for building in a milder climate.

Machinery and equipment costs are about the same as in Canada, but financial costs are lower.

However, Canada retains an advantage in terms of unit costs of energy, but this advantage is only marginal in view of the savings in energy for a plant location in a warm climate.

3. In southeastern United States, transportation costs of raw materials for the textile industry located there are minimal, since cotton and man-made fibers are also produced locally.

The transportation costs of finished products have also become more favourable than in Canada, following deregulation of transportation rates.

Under these conditions, it would likely be more advantageous to set up new production facilities or gradually relocate some activities in southern United States in preference to Canada. Those activities which would be most likely to benefit from such relocation are those for which there is no particular advantage in being located near its clients. This would be the case for yarn spinning, fabric weaving and knitting, and manufacturing of standardized garments (jeans, shirts, hosiery, underwear, etc.).

4. Canadian subsidiaries of American firms would have to undergo major adjustments. Where the production costs of these subsidiaries are similar to those in the American plants, the probable tendency would be towards much more specialization than at present. Where production costs are higher in Canada than in the United States, the maintenance of Canadian plants would be questionable. This would be inevitable for those industry sectors where there is overall excess capacity, which is the case for certain man-made fibres.

The arrangement for the automotive industry resolved the problem of Canadian subsidiaries of American firms by requiring commitments by the parent companies to maintain investments, production and employment in proportion with their total sales in Canada. Similar commitments for the textile and clothing industries would be more difficult to apply since there are only a few American firms with Canadian subsidiaries in these

industries, whereas in the automotive industry all the firms have subsidiaries.

5. Many Canadian firms, particularly in the clothing industry, carry out a substantial amount of business by producing under licence certain items with an international trade name. These licencing agreements will, for a fee, allow the exclusive use of an American or international trade mark for the period stated in the agreement.

In a free trade area, the future of licenced producers would be jeopardized. There is no major reason to prevent the American companies owning trademarks from taking back their exclusive licences. Since free trade effectively allows free movement of goods without having to pay duty, there would be no further need for a licencing agreement.

Licences from producers in other countries than the United States could also be in danger; only one licenced producer for North America would be required to satisfy the demand. The owner of the trademark, often a designer in a third country, could, because of the relative sizes of the Canadian and United States markets, give to only one manufacturer in the United States the exclusive rights to produce and distribute items bearing his trademark.

6. Canadian producers are somewhat apprehensive with regard to non-tariff barriers. In their opinion it would be important that these barriers be unified and their interpretation made uniform in both countries.

In this respect, mention was made of labelling regulations and in regulations concerning the flammability of products, where there are

important differences concerning children's clothing. Mention was also made of anti-dumping laws: Canadian producers fear that in the event they are successful in selling their products in the United States, they could be accused of dumping practices by their American competitors.

The Canadian producers would also like to be assured that interpretation of rules concerning the determination of value for duty be identical in both countries, and that rules on domestic content of products be applied uniformly. They expect also that administrative delays be cut to a minimum. There are actually some Canadian exporters who, in 24 to 30 months of export activity, have not succeeded in obtaining a single definitive tariff ruling from the United States customs authorities. In a free trade area the interpretation of domestic content rulings of exported products could suffer from the same delays and cause the same uncertainties.

Finally, many Canadian producers are afraid of "Buy American" campaigns. They consider, rightly or wrongly, that these campaigns are much more efficient in the United States than in Canada, and they see in this a major non-tariff barrier.

7.       Marketing of their products in the United States constitutes a major challenge for many Canadian producers. While American products are generally well known in Canada because of the numerous American fashion magazines distributed here and of the televised American publicity reaching this side of the border, American retailers and consumers know little or nothing about Canadian products and trade names because the medias of this country do not reach the American public.

Efficient marketing requires first a product with a "difference", and only a sales organization equal to or better than those of U.S. manufacturers would enable Canadian manufacturers to earn the trust of U.S. distributors and retailers.

There are very few Canadian manufacturers who can boast of having such "different" products. Most of them would have to develop novel products which would allow them to find a niche within the free trade area. Moreover, very few Canadian manufacturers have researched the U.S. market and tried to set up a distribution system in it. Their efforts were apparently blocked either by the ornamentation clause of the U.S. customs tariff which results in prohibitive duty levels, or by the need to invest considerable funds in a sales network and in advertising, funds which they rarely have under the present conditions.

However, some Canadian manufacturers have succeeded in penetrating the U.S. market. In most cases it involved products which were highly differentiated in terms of quality and design, and/or products often subject to relatively low U.S. duty rates.

8. The Canadian producers consider that a project of such scope as free trade with the United States must be linked with a temporary assistance program for industry covering several aspects of industry activity.

First, the program should provide investment assistance in a manner similar to the present program of the Canadian Industrial Renewal Board. Such assistance would ensure that the textile and clothing industries could make the necessary investments to reorganize their production.

Second, there should be provision for a marketing assistance program. This program would partially cover the costs of studies of selected markets, of shows and publicity, as well as part of the costs of setting up consortia or sales offices.

Third, the program would provide design assistance. Many producers feel that design should be considered as part of the industry infrastructure on the same basis as equipment. In making design less costly for the producer, the program would ensure the generalization of good design in the same way that CIRB ensures at present the generalization of advanced production technologies.

A good number of producers have emphasized the fact that creation of a free trade area should be accompanied by the stabilization of textile and clothing imports from low-cost countries. Indeed, it appears to them that it is difficult to face two challenges at the same time. If the erosion of their markets continues at the present rate they would not be able to generate sufficient funds to adjust in preparation for the implementation of free trade.

9. All the participants expressed their opinions regarding the transition period which they considered necessary to change from the current situation to that of freer movement of products between the two countries.

A small minority of participants, generally those who are already selling a significant proportion of their production in the United States, did not see the necessity for a transition period and said they were ready overnight or with minimum prior notice to enter into a free trade arrangement.

In contrast, other producers have suggested much longer transition periods of 3, 5, 10 or even 15 years, the duration of the transition period suggested depending on the degree of adjustment required.

The representations concerning the transition period brought out two major dilemmas for which the participants could see no solution.

The first dilemma concerns the timing of the transition periods in the textile and clothing industries. Most of the participants recognized that adjustment in the textile industry would be more difficult and take more time than in the clothing industry. However, it would be preferable for the clothing industry to benefit from free trade in textiles before liberalization of trade in clothing is undertaken. If the transition period for clothing were to start only at the end of the transition period for primary textiles the total transition period would be too long to be efficient.

The second dilemma relates to the transition periods in the United States and in Canada. The Canadian manufacturers consider that the burden of adjustment would fall on them only, the U.S. producers having little or no adjustment to make to serve the Canadian market. Also, since Canadian producers would have to fight hard to make their products known and accepted in the United States while their U.S. counterparts would not find such obstacles in their path, many participants have concluded that the United States should open their borders immediately to Canadian textile and clothing products while Canada should have the advantage of a transition period of several years during which Canadian tariff barriers would be lowered progressively.



## **CONCLUSION**

The oral and written presentations of the participants have generally allowed identification of the advantages of a free trade area between Canada and the United States. They also have brought in evidence the disadvantages and the risks of such a project. Some sub-sectors are convinced that they would come out winners. Others, as numerous and maybe more so, are convinced of the opposite. Again, others perceive a possible net advantage for their operations on condition that they gradually abandon their production in Canada and transfer it to the United States.

## APPENDIX I

### LIST OF PARTICIPANTS TO THE STUDY WHO PRESENTED BRIEFS TO THE BOARD AND/OR APPEARED AT PRIVATE HEARINGS

	<u>Brief</u>	<u>Hearing</u>
Aero Garment Limited	x	x
Amalgamated Clothing & Textile Workers Union	x	x
Apparel Manufacturers Association of Ontario	x	x
Ballin Inc.	x	x
Barry Manufacturing Company Limited	x	x
Bay Mills Ltd.		x
Bell Tootal Inc.	x	x
Bermatex Inc.		x
Bernard Cowan Inc.		x
Britex Ltd.		x
Brodkin Industries Inc.		x
Canadian Apparel Manufacturers Institute	x	x
Caulfeild, Burns and Gibson Limited		x
Children's Apparel Manufacturers' Association	x	x
Canadian Carpet Institute	x	x
Canadian Textiles Institute	x	x
Celanese Canada Inc.	x	x
Centrale des Syndicats Démocratiques	x	x
Century 21 Apparels Ltd.	x	x
Claudel Inc.		x
Cleyn & Tinker Inc.		x
Cluett, Peabody Canada Inc.	x	x

	<u>Brief</u>	<u>Hearing</u>
Commonwealth Curtain Co.		x
Consoltex Canada Inc.	x	x
Consumers' Association of Canada	x	
Coppley, Noyes & Randall, Limited	x	x
Dan Heap, M.P. for Spadina	x	x
Dance Originals and Tailored Juniors	x	x
Dominion Textile Inc.	x	x
DuPont Canada Inc.	x	x
Dylex Limited	x	x
Elite Blouse & Skirt Mfg. Ltd.	x	x
Forsyth Tradidng Co.		x
Gemini Fashions of Canada Ltd.	x	x
George Sheard Canada Inc.		x
Grand National Trouser Inc.	x	x
Hanson-Mohawk Inc.		x
Harvey Woods Limited	x	x
Huntingdon Mills Ltd.	x	x
International Ladies' Garment Workers' Union	x	x
Jantzen Canada Inc.		x
Jones Tent & Awning Limited	x	x
K-Brand Ltd.	x	
Koret Canada Inc.	x	x
Kovac Manufacturing Inc.	x	x
L. Davis Textiles Co. Ltd.		x
L.W.L. Ltée	x	
Lindzon Limited	x	x
Lutfy Ltd.	x	
Marquesa Fashions Inc.	x	
Midwest Garments Corporation		x
Monaco Group Inc.		x

	<u>Brief</u>	<u>Hearing</u>
Montreal Dress and Sportswear Manufacturers Guild		x
Montreal Fast Print Ltd.		x
Morbern Inc.		x
Nalpac Inc.		x
Nova Scotia Textiles, Limited		x
Patons & Baldwins Canada Inc.	x	x
Paulman International		
Div. of Weston Apparel Manufacturing Company		x
Peerless Clothing Inc.	x	x
Rice Sportswear Ltd.		x
Riviera Slacks Inc.	x	x
Satexil Inc.		x
Silknit Ltd.		x
Silpit Industries Co. Ltd.	x	x
Standard Knitting Ltd.		x
Stanfield's Limited	x	x
Stephen Kape Industries Inc.		x
Surrey Classics Manufacturing Limited		x
Tan Jay International Ltd.	x	x
Taran Furs Inc.		x
Textiles Dionne Inc.		x
Toronto Dress & Sportswear Manufacturers		
Guild Inc.		x
Toronto Ontario Designers		x
Wabasso Inc.	x	x
Warren K. Cook Limited		x
Wescott Fashions Ltd.		x
West Coast Woollen Mills Ltd.	x	x
Western Glove Works Ltd.	x	x

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